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STATE PASS CEA FOR BLOCK  
STATE PASS FEDERAL RESERVE BOARD FOR JOHNSON/SCHINDLER  
STATE PASS SAN FRANCISCO FRB FOR CURRAN  
STATE PASS NEW YORK FRB FOR DAGES/CLARK  
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SUBJECT: Guangdong Development Bank: A Benefit or a Burden?

REFERENCE: Guangzhou 30413

(U) This message is sensitive but unclassified. Please handle accordingly.

¶1. (SBU) SUMMARY: Citibank's Guangzhou branch manager said the Citibank-led bid for Guangdong Development Bank (GDB) is a "done deal" and that Citibank will gain significant management control over GDB as a result. Bank of America and Deutsche Bank representatives said Citibank would benefit from GDB's extensive branch network in the Pearl River Delta, but differed on whether it would gain the management control it wants. Media commentators opined that GDB was one of the last good investments for foreign banks and doubted that China would raise its foreign ownership cap anytime soon. END SUMMARY.

#### Background on the Deal

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¶2. (SBU) GDB was founded in 1988 by the Guangdong provincial government and was one of the earliest joint-stock commercial banks to offer a full range of financial services nationwide. The bank reportedly has over 500 branches, primarily in Guangdong's booming Pearl River Delta, and total assets of almost RMB 400 billion. The bank's non-performing loan rate is reportedly close to 20 percent. In 2004, GDB offered up 85 percent of its shares to outside investors. Citigroup originally aimed to take 40 to 45 percent of the bank, but later revised its proposal to 20 percent after the State Council refused to make an exception to the foreign ownership cap of 20 percent.

#### Citibank's Guangzhou Branch: Guarded but Optimistic

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¶3. (SBU) Milson Lau, Citibank's Guangzhou Branch Manager, said that although the November 16 agreement reached between the Citibank-led consortium and Guangdong Development Bank is a preliminary agreement, it represents a "done deal" and has the tacit approval of the Guangdong and central governments. The signed agreement includes a list of terms that must be met before a final agreement is reached in December 2006, including capital transfers, but Lau did not see them as barriers. He characterized the deal as the first time a foreign bank has taken significant management control of a domestic bank. He was careful to note, however, that he was not part of Citibank's GDB task force, nor is he closely acquainted with GDB managers. Regarding impending management changes in GDB,

Lau did not provide specifics but did say they would likely take place at high levels.

#### Other Foreign Banks: Mixed Reviews

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14. (SBU) Julia Yu, Bank of America's Guangzhou branch manager, said she expects that Citibank will have significant management control over GDB. She contrasted this with Bank of America's relationship with China Construction Bank (of which Bank of America owns nine percent). According to Yu, Bank of America is not involved in CCB's management, but rather provides training to branch-level offices on issues such as retail business. She noted that China Construction Bank is a national-level bank, and thus less flexible than a regional bank such as GDB. She expressed some surprise that Chinese authorities approved the deal, characterizing Citibank as a "tiger." She said Citibank's primary objective in the deal is to obtain GDB's extensive branch network.

15. (SBU) Myron Shi, Deutsche Bank's Guangzhou branch manager, said GDB will prove to be an enormous burden for Citibank and will not generate the profits that some expect. With new foreign banking regulations released on November 15 (see septel), Shi said foreign banks are better off opening wholly foreign-owned branches and sub-branches on their own terms. He noted that Deutsche Bank bought 10 percent of regional bank Huaxia in early 2006 but has not gained significant management control. In addition, he cited conversation with managers from the Bank of Communications in which they downplay the role of shareholder HSBC in day-to-day operations.

#### Media: Time to Look Further Afield

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16. (SBU) According to an article on China Finance Net, (a news

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website that is overseen by the People's Bank of China and the China Banking and Regulatory Commission) GDB is one of the last significant Chinese banks without a foreign partner. Most joint stock commercial banks with assets of between RMB 300 billion and RMB 500 billion already have foreign stakeholders. In the future, it says, foreign banks may look to agricultural commercial banks as new investment targets. The article cites sources close to the bidding process saying that 2006 will not see China ease the 20 percent cap on a single foreign investor in a domestic bank.

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